Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
1998 Biennial Regulatory Review --	)	
Review of Depreciation Requirements	)	CC Docket No. 98-137
	)	
	)	
Ameritech Corporation Telephone	)	CC Docket No. 99-117
Companies' Continuing Property Records	)	
Audit, *et. al.*	)	
	)	AAD File No. 98-26
GTE Telephone Operating Companies	)	
Release of Information Obtained During	)	
Joint Audit	)	

Comments

The National Exchange Carrier Association, Inc. (NECA) submits these Comments on the Commission's *Further Notice of Proposed Rulemaking* in the above captioned matter.[1] This proceeding is intended "to evaluate the conditions under which [the Commission's] existing depreciation rules may be eliminated or changed for all price-cap carriers,"[2] in a manner that serves the public interest. In making this evaluation, the Commission seeks comment, among other things, on the effects of a five-year amortization proposal, by which the differential between carriers' financial and regulatory books would be eliminated.

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[1] *See* 1998 Biennial Regulatory Review -- Review of Depreciation Requirements for Incumbent Local Exchange Carriers, CC Docket No. 98-137, Ameritech Corporation Telephone Operating Companies' Continuing Property Records Audit, *et.al.*, CC Docket No. 99-117, GTE Telephone Operating Companies Release of Information Obtained During Joint Audit, AAD File No. 98-26, *Further Notice of Proposed Rulemaking*, FCC 00-119, rel. Apr. 3, 2000 (*FNPRM*).

[2] *Id.* at ¶ 2 (note omitted.)

I. Introduction and Background

In the context of the Commission's *Depreciation Order*,[3] ILEC (incumbent local exchange carrier) members of the Coalition for Affordable Local and Long Distance Services (CALLS) proposed, over the life of the CALLS plan,[4] to take steps "to eliminate the disparity that exists between the regulatory and the financial accounting for depreciation expense and associated reserve balances."[5] These steps would be initiated by grant of a ILEC joint request for waiver of the Commission's depreciation rules, pursuant to the *Depreciation Order*.[6]

The *FNPRM* identifies four requirements necessary for granting such waivers.[7] These requirements were established, in part, so that it (the Commission) could "continue to establish ranges for use in cost models," and because of its concern that new

[3] *See* 1998 Biennial Regulatory Review - Review of Depreciation Requirements for Incumbent Local Exchange Carriers, *Report and Order in CC Docket No. 98-137*, 15 FCC Rcd 242 (2000)(*Depreciation Order*.)

[4] *See FNPRM* at note 3.

[5] *Id.* at ¶ 2 and note 5. The Commission cites a letter from CALLS ILEC member representatives to Lawrence Strickling, Chief, Common Carrier Bureau, dated March 3, 2000, in which these ILEC members state their intention to file a joint request for waiver of the Commission's depreciation requirements (*CALLS ILEC Letter*).

[6] *Id.*

[7] *Id.* The Commission identified the following conditions for granting waivers of its depreciation rules. "(When) an ILEC voluntarily, in conjunction with its request for waiver: (1) adjusts the net book costs on its regulatory books to the level currently reflected in its financial books by a below-the-line write-off; (2) uses the same depreciation factors and rates for both regulatory and financial accounting purposes; (3) forgoes the opportunity to seek recovery of the write-off through a low-end adjustment, an exogenous adjustment, or an above-cap filing; and (4) agrees to submit information concerning its depreciable plant accounts including forecast additions and retirements for major network accounts and replacement plants for digital central offices."

depreciation methods might have adverse or unintended effects on cost models used to determine universal service high cost loop support.[8]

> (T)he current depreciation prescription process is important in the calculation of high cost support amounts because it provides the input for the depreciation expense component of the carriers' average costs per loop. An increase in these expenses by large ILECs could lead to reductions in the high cost support for other, primarily rural, carriers, many of which rely on high cost support to keep their local rates affordable.[9]

Further, the Commission noted its intention to "maintain realistic ranges of depreciable life and salvage factors for each of the major plant accounts" in order to, among other things, "prevent any inappropriate fluctuations in high cost support."[10]

II. Discussion

The Commission prescribes depreciation factors used by price cap ILECs whose revenues exceed an indexed revenue threshold, presently set at annual revenues of $112 million.[11] Recently adopted Commission rules also specify that non-rural carriers' high cost support is the larger of (1) an amount determined via previous USF calculation methods, *i.e.*, basing the amount of support on the comparison between the carrier's average cost per loop and the nationwide average cost per loop,[12] or (2) an amount

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[8] *See FNPRM* at ¶ 8 (note omitted).

[9] *Id.*

[10] *Id.*

[11] *See Depreciation Order* at ¶ 3.

[12] *See* Federal-State Joint Board on Universal Service, *Ninth Report & Order and Eighteenth Order on Reconsideration*, CC Docket No. 96-45, 14 FCC Rcd 20432 (1999), (*Ninth Report and Order on Universal Service*) at ¶¶ 78-88.

determined via the new synthesis model.[13] In the *Depreciation Order*, the Commission clearly stated its concern about changes in its depreciation prescription process, and the need to understand the effects of such changes on the universal service high-cost support process.

> If these carriers were to use their financial depreciation factors for regulatory purposes, they would report major increases in their average costs per loop. This would increase substantially their high cost support under method (1) [*supra*]. Under this method, however, because high cost support is subject to a cap, increases in the largest incumbent LECs' high cost support would not increase the fund. Instead, it would lead to substantial reductions in the high cost support for other, primarily rural, carriers, many of which rely to a great extent on high cost support to keep their local rates affordable.[14]

NECA shares the Commission's concern about the potential effects of these changes on high cost support. Analysis of USF payments that would result from changes in the calculation of high cost support as a result of modified depreciation methods and reserve balances confirms the Commission's observation. In a "capped" fund environment, payments to rural carriers in particular could be significantly reduced, or, in some cases, eliminated. Also, because *all* ILECs' (including price cap companies) loop costs are used to develop the national average cost per loop, even in an uncapped

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[13] *See* Federal-State Joint Board on Universal Service, Forward-Looking Mechanism for High Cost Support for Non-Rural LECs, *Tenth Report and Order*, CC Docket Nos. 96-45 and 97-160, 14 FCC Rcd 20156 (1999)(*Tenth Report and Order on Universal Service*) at ¶¶ 419-431.

[14] *See Depreciation Order* at ¶ 29.

environment, the change in depreciation methodology will produce lower support amounts for rural carriers.

Reasonable methods may be employed to prevent these possible adverse effects on high cost funding. For example, the Commission could establish procedures to be used to satisfy the reporting requirements of section 36.611 of its rules,[15] by which it would "freeze" the investment and depreciation expense-per-loop components for price cap companies electing to use these alternative depreciation methods. The frozen per-loop amounts could then be used, on a going-forward basis, to impute universal service high cost requirements and study area loop costs, based on changes in loop counts. Another possible alternative would be to use currently available data to establish a 3 or 5-year historical average amount of depreciation expense and investment per loop, as surrogates for use in calculating these companies' study area loop costs and the national average loop cost. Other reasonable alternatives may exist as well. Should the Commission determine that changes in its depreciation rules are in the public interest, NECA strongly urges the Commission to consider adopting a reporting method that will avoid adverse impacts on high cost funding amounts.

The Commission should also consider eliminating the interim cap on the high cost fund. As has been demonstrated in the context of other proceedings,[16] shortfalls resulting

[15] Section 36.611 specifies information reporting requirements imposed on all ILECs for purposes of determining universal service fund expense adjustment payments, including, in part, depreciation expense and accumulated depreciation. *See* 47 C.F.R. § 36.611.

[16] *See* Inquiry Concerning Deployment of Advanced Telecommunications Capability to all Americans in a Reasonable and Timely Fashion, And Possible Steps to accelerate Such Deployment Pursuant to Section 706 of The Telecommunications Act of 1996, CC Docket No. 98-146, *Notice of Inquiry*, NECA *Comments*, (Mar.17, 2000) at 6-8; and Federal-State Joint Board on Universal Service: Promoting Deployment and

from the interim cap have reached alarming levels – over $130 million in 2000 funding alone.[17]

As noted above, NECA and others have repeatedly expressed concerns about the impact of the cap in the Commission's Universal Service, Interconnection, and Access Charge Reform proceedings, among others. The cap hinders key Commission (and telephone industry) objectives: universal service, advanced services deployment, and deployment to unserved/under-served areas. Full funding of universal service will serve the public interest as a critical first step in achieving rapid deployment of broadband services, and will help bridge the "digital divide."

III. Conclusion

NECA believes that changes in depreciation methods may have a potentially significant effect on universal service funding. The effect of the change would be exacerbated by the "interim" cap on the fund. The Commission thus should consider alternatives that would insulate the Section 36.621[18] high cost fund from the effects of

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Subscribership in Unserved and Underserved areas, Including Tribal and Insular Areas, CC Docket No. 96-45, *Further Notice of Proposed Rulemaking, Joint Comments* of NECA and United States Telecom Association, (Dec. 17, 2000) at 4-6; and Federal-State Joint Board on Universal Service, Common Carrier Bureau Seeks Comment on Requests to Redefine "Voice Grade Access" for Purposes of Universal Service Support, CC Docket No. 96-45, *Public Notice*, NECA *Comments*, (Jan.19, 2000) at 3-6; and Access Charge Reform , Price Cap Performance Review for Local Exchange Carriers, Low-Volume Users, and the Federal-State Joint Board on Universal Service, CC Docket Nos. 96-262, 94-1, 99-249, and 96-45, Coalition for Affordable Local and Long Distance Services (CALLS) Modified Proposal, National Telephone Cooperative Association, Inc. *Comments* (Apr. 3, 2000) at 11.

[17] *See* Universal Service Fund Submission of 1998 Study Results by the National Exchange Carrier Association, (Oct. 1, 1999), at 5.

[18] *See*, generally, 47 C.F.R. § 36.621 which specifies the formula for calculating study area total unseparated loop cost.

changes in its depreciation rules. Additionally, the Commission should remove the "interim" cap on the universal service fund. The cap hinders the Commission's universal service goals by preventing full cost recovery for many rural carriers and by distorting the effects of otherwise reasonable proposals to streamline Commission regulation of depreciation practices.

Respectfully submitted

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<u>CERTIFICATE OF SERVICE</u>

I hereby certify that a copy of the foregoing Comments was served this 17th day of April 2000 by electronic delivery or US mail to the persons listed below.

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